

June 13, 2014

Investment Grade Credit

## European Banks

### When Will Crédit Agricole Call Its Non-Steps?

**We were initially surprised by Agricole's call of its retail non-step \$550m 7% earlier this year, but this entirely fits with a strategy of maximizing grandfathering buckets. Analysing its €9.3bn of 'grandfatherable' Tier 1s, we believe the \$1.5bn 7% prefs should not be called before 2017, and the €6% €550m even later.**

**We took Agricole's €9.3bn of Tier 1 as at FY12** as our starting point (disclosed by the EBA), which is its maximum grandfathering amount, and reconciled it with individual bonds, as shown in Exhibit 1 overleaf. Taking the grandfathering limit to 80% for this year, Agricole currently has an 'excess' of €750m. Looking at the most expensive bonds outstanding (coupons) and the excess to neutralise, we assume the bank will call its \$1.35bn 9.75% in December.

**In FY15, we expect Agricole to call its \$500mn 7.375% prefs**, according again to the grandfathering limit (then down to 70%), taking into account our assumption of FY14 calls and also Tier 1s with step-ups in FY15, which will cease to get grandfathering value.

**The \$1.5bn 7% should be called in FY17** according to the analysis running forward, and for the €550m 6%, it could well be that this remains outstanding to the end of the grandfathering period (2022). This is because Agricole has a number of step-up Tier 1s in 2018 and 2019 which will cease to be grandfathered, and 'open up' the limit, to be filled by non-called non-steps.

**We remain buyers of the \$7% and €6%**, with spreads to expected call dates of 30 January 2017 for the 7% and, conservatively, 30 January 2018 for the 6% at z+556bp (6.4% YTC) and z+531bp (5.8% YTC). See Exhibit 3 on page 3 for a call date scenario analysis.

#### MORGAN STANLEY RESEARCH

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#### Trade recommendations

|        |        |     |     |          |        | YTC(%) to 30-Jan of: |      | Z-t-C to 30-Jan of: |      |
|--------|--------|-----|-----|----------|--------|----------------------|------|---------------------|------|
| Ticker | Type   | Ccy | Cpn | Maturity | Offer  | 2017                 | 2018 | 2017                | 2018 |
| ACAFP  | Tier 1 | \$  | 7   | Perp     | 101.40 | 6.4                  | 6.6  | 556                 | 531  |
| ACAFP  | Tier 1 | €   | 6   | Perp     | 100.7  | 5.7                  | 5.8  | 533                 | 531  |

Source: Bloomberg, Morgan Stanley Research

#### Risk Factors

Choice of bonds to call will not only be influenced by grandfathering and coupon cost; other factors will be how the Tier 1 has been hedged (swap gains), or choice of currency, future leverage ratio requirements and cost of issuing AT1 as a replacement.

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Exhibit 1

**Crédit Agricole: Legacy Tier 1 Grandfathering Scenario Analysis**

| In EUR million   | 2014        | 2015       | 2016       | 2017       | 2018      | 2019        | 2020      | 2021       | 2022 | 2023 | 2024  | 2025 | 2026 |
|--|-------------|------------|------------|------------|-----------|-------------|-----------|------------|------|------|-------|------|------|
| Step-up  |             | 329        | 289        | 40         | 1,350     | 1,653       | 215       |            |      |      |       |      |      |
| Non-step   | 3,025       | 371        | 120        | 817        |           |             |           |            |      |      |       |      |      |
| AT1  |             |            |            |            |           |             |           | 1,000      |      |      | 1,293 |      | 626  |
| T1 grandfathering allowance  | 7,450       | 6,519      | 5,588      | 4,656      | 3,725     | 2,794       | 1,863     | 931        |      |      |       |      |      |
| Old T1 securities outstanding at end of year if no non-step called                           | 8,211       | 6,885      | 6,226      | 6,186      | 3,727     | 2,074       | 1,859     | 1,859      |      |      |       |      |      |
| Excess T1 end of year if no non-steps called this year                                       | 761         | 365        | 638        | 1,529      | 2         | -720        | -4        | 927        |      |      |       |      |      |
| Non-step T1s calls expected scenario   | 997         | 369        |            | 1,108      |           |             |           |            |      |      |       |      |      |
| Expected date of non-step call   | 12/26/2014  | 04/19/2015 |            | 01/30/2017 |           |             |           |            |      |      |       |      |      |
| <b>Excess T1 end of year over grandfathered limit under non-step calls expected scenario</b> | <b>-245</b> | <b>-11</b> | <b>631</b> | <b>416</b> | <b>-2</b> | <b>-722</b> | <b>-6</b> | <b>925</b> |      |      |       |      |      |

Source: Morgan Stanley research, Bloomberg, Crédit Agricole; AT1 is not included in legacy Tier 1s.

Exhibit 2

**Crédit Agricole T1 Hybrid Securities**

| Security              | ISIN         | Step/Non-step/AT1 | Step-up date | Next call date | Amount in ccy | Currency | Amount in EUR |
|-----------------------|--------------|-------------------|--------------|----------------|---------------|----------|---------------|
| ACAFF 7 10/29/49      | XS0173838847 | Non-step          |              | Called         | 0             | USD      | 0             |
| ACAFF 7 01/29/49      | XS0161441000 | Non-step          |              | 30/07/2014     | 1,500,000,000 | USD      | 1,108,319,787 |
| ACAFF 6 12/29/49      | NL0000113868 | Non-step          |              | 30/07/2014     | 550,000,000   | EUR      | 550,000,000   |
| ACAFF 7 3/8 10/29/49  | FR0010533554 | Non-step          |              | 19/10/2014     | 500,000,000   | USD      | 369,439,929   |
| ACAFF 9 3/4 06/29/49  | FR0010772244 | Non-step          |              | 26/12/2014     | 1,350,000,000 | USD      | 997,487,808   |
| ACAFF 0 12/29/49      | FR0010161026 | Non-step          |              | 04/02/2015     | 371,232,000   | EUR      | 371,232,000   |
| ACAFF 4.13 11/29/49   | FR0010248641 | Step              |              | 09/11/2015     | 328,950,000   | EUR      | 328,950,000   |
| ACAFF 5.136 12/29/49  | FR0010291997 | Step              | 02/24/2016   | 24/02/2016     | 198,600,000   | GBP      | 248,763,074   |
| CARPP 0 06/29/49      | IT0004743818 | Non-step          |              | 6/28/2016      | 120,000,000   | EUR      | 120,000,000   |
| ACAFF 5 1/2 08/29/49  | FR0010359794 | Step              | 08/11/2016   | 11/08/2016     | 59,700,000    | CAD      | 40,619,429    |
| ACAFF 6.637 05/29/49  | US225313AA37 | Non-step          |              | 31/05/2017     | 889,928,000   | USD      | 657,549,874   |
| CACEIS 6.315 perp     | -            | Step              | 11/28/2017   | 11/28/2017     | 40,000,000    | EUR      | 40,000,000    |
| ACAFF 5.04 12/29/49   | NZCASD0001S5 | Non-step          |              | 19/12/2017     | 250,000,000   | NZD      | 159,907,893   |
| ACAFF 8.2 03/29/49    | FR0010603159 | Step              | 03/31/2018   | 31/03/2018     | 850,000,000   | EUR      | 850,000,000   |
| ACAFF 10.653 09/29/49 | FR0010670422 | Step              | 09/30/2018   | 30/09/2018     | 500,000,000   | EUR      | 500,000,000   |
| ACAFF 8 3/8 10/29/49  | USF22797FK97 | Step              | 10/13/2019   | 13/10/2019     | 1,000,000,000 | USD      | 738,879,858   |
| ACAFF 8 1/8 10/29/49  | FR0010814418 | Step              | 10/26/2019   | 26/10/2019     | 291,050,000   | GBP      | 364,564,414   |
| ACAFF 7 7/8 10/29/49  | FR0010814434 | Step              | 10/26/2019   | 26/10/2019     | 550,000,000   | EUR      | 550,000,000   |
| ACAFF 7.589 01/29/49  | FR0010575654 | Step              | 01/30/2020   | 30/01/2020     | 171,850,000   | GBP      | 215,256,466   |
| ACAFF 6 1/2 06/23/49  | XS1055037177 | AT1               |              | 23/06/2021     | 1,000,000,000 | EUR      | 1,000,000,000 |
| ACAFF 7 7/8 01/29/49  | USF22797RT78 | AT1               |              | 23/01/2024     | 1,750,000,000 | USD      | 1,293,039,752 |
| ACAFF 7 1/2 04/29/49  | XS1055037920 | AT1               |              | 23/06/2026     | 500,000,000   | GBP      | 626,291,727   |

Source: Bloomberg, Crédit Agricole

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Exhibit 3

## Call Date Scenarios for the Crédit Agricole \$7% and the €6%

| ISIN         | Type   | Ccy | Ticker | Cpn | Next Call  | Maturity | Amt os (m) | Offer | YTC (%) | Z-t-C | YTC(%) to the beginning of: |      |      |      | Z-t-C to the beginning of: |      |      |      |
|--------------|--------|-----|--------|-----|------------|----------|------------|-------|---------|-------|-----------------------------|------|------|------|----------------------------|------|------|------|
|              |        |     |        |     |            |          |            |       |         |       | 2015                        | 2016 | 2017 | 2018 | 2015                       | 2016 | 2017 | 2018 |
| XS0161441000 | Tier 1 | \$  | ACAPF  | 7   | 30-07-2014 | Perp     | 1,500      | 101.4 | -4.9    | -510  | 4.7                         | 6.1  | 6.4  | 6.6  | 443                        | 563  | 556  | 531  |
| NL0000113868 | Tier 1 | €   | ACAPF  | 6   | 30-07-2014 | Perp     | 550        | 100.7 | 0.0     | -26   | 4.7                         | 5.5  | 5.7  | 5.8  | 435                        | 521  | 533  | 531  |

Source: Bloomberg, Morgan Stanley Research

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